

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

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FEDERAL COMMUNICATIONS COMMISSION
OFFICE OF THE SECRETARY

In the Matter of)
Implementation of Pay Telephone)
Reclassification and Compensation)
Provisions of the Telecommunications)
Act of 1996)

CC Docket No. 96-128

COMMENTS OF THE CONSUMER-BUSINESS
COALITION FOR FAIR PAYPHONE 800 FEES

The Consumer-Business Coalition for Fair Payphone 800 Fees ("Consumer-Business Coalition"),^{1/} by its attorneys and pursuant to the Commission's June 19, 1998 Public Notice in the above-referenced proceeding,^{2/} hereby submits its comments on the issues raised by the D.C. Circuit Court's remand^{3/} of the Commission's Second Report and Order^{4/} on payphone reform. As described more fully below, the Commission should heed the D.C. Circuit's clear directive and abandon its attempt to link the rate for 800 and access code payphone calls to the local coin rate. The Commission should instead adopt an incremental cost-based approach to pricing

^{1/} The Consumer-Business Coalition is an organization of business and consumer groups that are reliant on affordable 800 service being available from payphones and are adversely affected by the Commission's current pricing methodology. It's members include: the AAA, American Trucking Associations, Air Transport Association, American Airlines, American Moving and Storage Association, Citicorp., Consumer Federation of America, Ecolab, International Communications Association, Motel 6 Operating L.P., Nabisco, Inc., National Network to End Domestic Violence, Owner-Operator Independent Drivers Association, Small Business Legislative Council, Transportation Intermediaries Association, Truckload Carriers Conference, and Virtual Voice Corporation.

^{2/} "Pleading Cycle Established for Comment on Remand Issues in the Payphone Proceeding," Public Notice, DA 98-1198 (rel. June 19, 1998) ("Public Notice").

^{3/} MCI Telecomm. Corp. v. Fed. Communications Comm'n, No. 97-1675, slip. op. (D.C. Cir. May 15, 1998).

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coinless calls so that payphone providers can be fairly compensated for the use of their phones without unduly harming 800 service subscribers, consumers and other payphone users.

INTRODUCTION AND SUMMARY

In its May 15, 1998 decision, the D.C. Circuit remanded for reconsideration the Commission's \$0.284 interim per-call compensation rate for 800 and dial-around payphone calls on the ground that the FCC failed to explain adequately how a fair rate for coinless calls could be derived by subtracting coin-specific costs from the \$0.35 rate charged for local coin calls.^{5/} Specifically, the Court noted that because the FCC failed to show how the market rate for coin calls accurately reflects the costs of those calls, the FCC's subtraction of coin-specific costs from the local coin rate was akin to "subtracting apples from oranges" and was "unreasoned."^{6/} The D.C. Circuit's dissatisfaction with the FCC was even more pronounced at oral argument, wherein phrases such as "utterly irrational" were used to describe the Commission's pricing methodology.^{7/}

In 1997, the first time the D.C. Circuit struck down the Commission's approach to pricing coinless calls, the Court found that the Commission's methodology "epitomize[d] arbitrary and capricious decisionmaking."^{8/} Now, despite being told for the second time by the D.C. Circuit that its rationale for using the local coin rate to calculate the coinless rate was

^{4/} In the Matter of Implementation of Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Second Report and Order, CC Docket No. 96-128, 13 FCC Rcd 1778 (1997) ("Second Report and Order").

^{5/} MCI Telecomm. Corp. at 6.

^{6/} Id. at 5.

^{7/} Transcript of Proceedings, MCI Telecomm. Corp. v. Fed. Communications Comm'n, No. 97-1675 (May 7, 1998) ("Transcript") at 32.

^{8/} Illinois Pub. Telecomm. Ass'n v. Fed. Communications Comm'n, 117 F.3d 555, 564 (D.C. Cir. 1997).

“plainly inadequate,”^{9/} the Commission appears to be barreling headfirst down the same path, insisting, or so it seems, that there must be some way to reconcile the coin and coinless markets to arrive at a coin-based rate for coinless calls.^{10/}

As has already been explained by the Consumer-Business Coalition in prior rounds of this proceeding, the fact is that the coin and coinless markets cannot be reconciled.^{11/} This is because competitive conditions do not yet exist in the payphone marketplace, nor is it likely that they ever will. Although, as described by the Commission, the payphone market is in fact replete with service providers,^{12/} these providers do not compete for customers on a point of sale basis. Therefore, the payphone marketplace cannot be said to be competitive. More importantly, even if, hypothetically speaking, competitive alternatives did exist in the payphone marketplace, basing the coinless rate on the local coin rate would be inappropriate because, unlike coin callers, end users placing 800-number payphone calls are not paying directly for those calls. 800-number payphone callers therefore do not exercise the same market discipline as coin callers that is necessary to move to a market rate.

^{9/} MCI Telecomm. Corp. at 5.

^{10/} See Public Notice at 2-3. The fact that the FCC’s Public Notice seeks comment on “the reasonableness of adjusting the local coin rate for cost differences between providing coin and coinless calls as a market-based mechanism for deriving fair compensation for coinless calls” suggests that the Commission has not given up on its ill-conceived plan to tie the coinless rate to the local coin rate. Id.

^{11/} See, e.g., Reply Comments of the Consumer-Business Coalition, CC Docket No. 96-128 (filed Jan. 20, 1998) at 3; Comments of the Consumer-Business Coalition, CC Docket No. 96-128 (filed Jan. 7, 1998) (“Consumer-Business Coalition Comments”) at 4; Petition for Reconsideration of the Consumer-Business Coalition, CC Docket No. 96-128 (filed Dec. 1, 1997) (“Consumer-Business Coalition Petition”) at 18.

^{12/} In the Matter of Implementation of Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Report and Order, 11 FCC Rcd 20541 (1996) (“First Report and Order”) at ¶ 11, fn. 24.

Despite the FCC's continued touting of call blocking as a magic elixir that will level the playing field and enable 800 subscribers to avoid paying unreasonable per call compensation rates, the inability of 800 service subscribers to block calls selectively on a per-phone basis significantly diminishes its value. Furthermore, most 800 subscribers are reliant on being accessible from all phones, including payphones, thereby rendering call blocking an invalid business option. It is for these reasons, in addition to others, that the Commission must abandon its twice-rejected premise that the coinless rate should be based on the local coin rate. The Commission should instead recognize the imperfections in the payphone marketplace and adopt an incremental cost-based rate for coinless calls that will be fair for everyone. Should the Commission change its approach to pricing coinless calls, it should also require that any refunds made to interexchange carriers ("IXCs") by payphone providers get passed through to 800 subscribers.

I. THE D.C. CIRCUIT HAS MADE IT ABUNDANTLY CLEAR THAT THE COINLESS RATE CANNOT BE BASED ON THE LOCAL COIN RATE

Section 276 of the Telecommunications Act of 1996 ("1996 Act") requires that payphone providers receive "fair compensation for each and every completed intrastate and interstate call."^{13/} To achieve this statutory mandate in the local coin market, the Commission simply deregulated the local coin rate.^{14/} The rate for non-coin calls presented a more difficult situation, however, because there has never been a "market" for coinless calls.^{15/} Rather than deliberately

^{13/} 47 U.S.C. § 276(b)(1)(A).

^{14/} See First Report and Order at ¶¶ 13-16. As a result of the Commission's action, the vast majority of payphone service providers increased their rate for local payphone calls to \$0.35.

^{15/} In other words, the pricing of coinless calls has not been determined by the principles of supply and demand. Interexchange carriers have typically paid a monthly flat rate for all 800 calls placed from payphones.

craft a rate for coinless calls using a bottom-up approach to pricing, the Commission decided to adopt the local coin rate as a “market surrogate” for coinless calls.^{16/}

Not surprisingly, the D.C. Circuit vacated and remanded the FCC’s decision on the ground that the Commission did not adequately justify linking the coin rate to the coinless rate.^{17/} In its first decision on this issue, the Court noted that the problem with the FCC’s adoption of a market surrogate for coinless calls was that the record was “replete with evidence that the costs of local coin calls versus 800 and access code calls are not similar.”^{18/} In response to the D.C. Circuit’s decision, the Commission in its Second Report and Order tried to distinguish the local coin rate from the coinless rate by deducting \$0.066 of coin-specific costs from the \$0.35 local coin rate. In essence, the Commission once again created a “market rate” – this time in the amount of \$0.284 – for coinless calls.

Finding the FCC’s approach to be completely “unreasoned” and akin to “subtracting apples from oranges,” the D.C. Circuit for the second time struck down the Commission’s methodology for pricing coinless calls.^{19/} This time, however, the Court gave the Commission only six months to correct the problem.^{20/} Thus, despite the FCC’s repeated convoluted attempts to link the coinless rate to the local coin rate, the D.C. Circuit has twice plainly ruled that the FCC cannot use one market to set the rate for another, and that costs cannot logically be deducted from rates when setting prices. Indeed, the Court’s frustration was readily apparent at oral

^{16/} See In the Matter of Implementation of Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, Order on Reconsideration, 11 FCC Rcd 21233 (1996) (“Reconsideration Order”) at ¶¶ 66-73; First Report and Order at ¶¶ 67-76.

^{17/} Illinois Pub. Telecomm. Ass’n, 117 F.3d at 564

^{18/} Id. at 563.

^{19/} MCI Telecomm. Corp. at 5.

^{20/} Id. at 7.

argument when phrases such as “makes no sense” and “utterly irrational” were used to describe the Commission’s skewed methodology.^{21/}

Notwithstanding the crystal clear directive by the D.C. Circuit that the coinless rate cannot logically be tied the price of a local coin call, the Commission still appears to be trying to base the former on the latter.^{22/} As described more fully below, however, a number of imperfections in the payphone market prevent the Commission from legitimately doing this. Indeed, the Commission itself has acknowledged that the existence of locational monopolies and the lack of pricing information available to non-coin callers at the point of sale creates considerable market distortions in the pricing of coinless calls.^{23/} In addition, as the Consumer-Business Coalition has pointed out numerous times in this proceeding, call blocking does not provide 800 subscribers with adequate protection from paying unreasonable per-call compensation rates. This is because call blocking cannot be exercised on a per-phone basis, thereby rendering it an “all or nothing” proposition, and, even if call blocking were available in this manner, most 800 subscribers could not use it because they rely on being accessible from all phones, including payphones.

Though not readily apparent in the language of the D.C. Circuit’s decision, the transcript of the oral argument makes clear that the Commission actually only narrowly escaped having its

^{21/} Transcript at 32-33.

^{22/} See Public Notice at 2-3. Specifically, the Commission’s current Public Notice seeks comment on “how the distinctions between [the coin and coinless markets] should affect the determination of a reasonable default compensation amount for coinless calls,” the “market imperfections that might affect the use of the local coin rate as a market-based surrogate for coinless calls,” and “the reasonableness of adjusting the local coin rate for cost differences . . . [to arrive at a] market-based mechanism” for coinless calls. Id.

^{23/} See First Report and Order at ¶¶ 13-16.

per-call compensation rate vacated for a second time.^{24/} The only thing that apparently prevented the Court from staying the FCC's purported "market approach" to pricing of coinless calls was an impassioned plea on the part of the independent payphone providers that, without some form of per-call compensation at this time, they would be severely harmed.^{25/} Ironically, by continuing to insist on linking the coinless rate to the local coin rate, the FCC is not only enhancing the likelihood of being overturned a third time, it is also running the risk of ultimately harming payphone providers – the very parties it ostensibly seeks to protect. Accordingly, it is vital that the Commission give serious consideration to the other options available for pricing coinless calls – including an incremental cost-based approach – so that payphone reform will endure and will ultimately benefit everyone.^{26/}

II. BASING THE RATE FOR COINLESS CALLS ON A "MARKET SURROGATE" WAS INAPPROPRIATE BECAUSE THE PAYPHONE MARKET IS NOT COMPETITIVE

The Commission's decision to deregulate the local coin rate and adopt a market surrogate for coinless calls was based largely on its finding that "the payphone industry has the potential to become very competitive."^{27/} This finding was premised on the fact that numerous payphone providers operate throughout the country, and that "[e]ntry into the payphone market appears to

^{24/} Transcript at 60.

^{25/} Id.

^{26/} Any claim that an incremental cost-based approach prevents payphone providers from recovering joint and common costs is without merit. As the Commission itself acknowledges, "a cost-based interconnection standard . . . compensates a carrier for the long run incremental cost of providing interconnection or the long run cost of providing an unbundled element *plus a reasonable share of the common costs.*" Implementation of the Pay Telephone Reclassification and Compensation Provisions of the Telecommunications Act of 1996, CC Docket No. 96-128, Second Report and Order, FCC 97-371 (rel. Oct. 9, 1997) at ¶ 95 (emphasis added); see also Consumer-Business Coalition Petition at 22-25.

^{27/} First Report and Order at ¶ 11.

be easy.”^{28/} Notwithstanding this overly-optimistic assessment, the fact is that real competition does not currently exist in the payphone marketplace. This is because the common practice by property owners of awarding locational monopolies to payphone providers in exchange for commissions prevents competition from flourishing on a point-of-sale basis.

Without location-by-location competition, the fact that “there are over 15,000 [payphone service providers]”^{29/} is irrelevant. Payphone users are still captive to the rate charged by a singular provider at the point of sale, and it remains virtually impossible to track down a payphone operated by an alternative provider. The Commission itself acknowledged this when it first adopted its compensation methodology, stating that locational monopolies significantly distort the payphone market, and that, absent regulation, a payphone service provider may have an incentive to charge supra-competitive prices.^{30/}

In light of its recognition that locational monopolies may prevent the payphone marketplace from becoming competitive, the Commission explicitly left open the possibility that additional regulation may be necessary.^{31/} Specifically, the Commission found that for 800 and dial around calls, a phased-in approach involving a default rate was warranted, and that during the first year of per-call compensation, the Commission should evaluate the deregulated local

^{28/} Id.

^{29/} Id. at fn. 24. It is worth noting that the payphone industry has undergone significant consolidation in recent months and that only one large independent payphone provider, Davel Communications Group, Inc., now exists to rival the size of the Regional Bell Operating Companies’ payphone affiliates. “Davel, PhoneTel Sign Merger Pact,” Davel Communications Group, Inc. Press Release (June 12, 1998) at 1 (<http://www.davelgroup.com/pr02.htm>). It is also worth noting that Davel paid a substantial premium over market price for its recent acquisition of PhoneTel. Id. at 2 (stating that “the merger consideration of \$3.08 per share is 64 percent over PhoneTel’s closing price Thursday’s of \$1.875 per share”).

^{30/} Id. at ¶¶ 15, 59.

^{31/} Id.

coin rate to determine whether significant market dysfunctions exist.^{32/} The problem with this approach is that the Commission looks only to the local coin rate for guidance as to whether the payphone market is operating in a healthy and competitive manner. Because significant differences exist between the coin and coinless markets, however, the former cannot properly be used as a bellwether for – or even be tied to – the latter.

In particular, while a caller placing a local coin call is well informed of the rate he or she will pay and, accordingly, exercises discretion in deciding whether to place the call, a caller placing an 800-number call is less likely to know, or care, about the rate that will be incurred because the caller is often not the one paying for the call. For example, a party requiring travel information at an airport may opt to call an airline's 800-number from a payphone instead of walking to an adjacent terminal to check an airport monitor.

This lack of market discipline on the part of the 800 caller is a significant market distortion that went unrecognized by the Commission in the First Report and Order and continues to plague 800 service subscribers. Although payphone providers may contend that this is the cost of making a company 800 number available from payphones, the fact is that the Commission explicitly sought to guard against this situation by enabling 800 subscribers to block calls from certain payphones. Specifically, the Commission recognized that 800 subscribers and dial-around users should be able to avoid paying for calls from payphones that are unduly expensive or located in places not connected to their business through call blocking.

Call blocking, however, is not a viable business option because blocking calls from specific payphones is not technically feasible at this time. It is the Consumer-Business Coalition's understanding that 800 service subscribers have the choice of blocking *all* calls from

^{32/} Id. at ¶¶ 15, fn. 31; 51.

all payphones or blocking no calls at all. This is not really a “choice” and, in any event, it surely does not provide 800 service subscribers with any bargaining leverage over payphone providers. Moreover, because many 800 subscribers are dependent upon being accessed from all phones, they cannot, for business and public interest reasons, block any calls and are captive to whatever rate is demanded. The notion that the payphone market is sufficiently competitive to permit a market rate to exist for coinless calls is therefore ill-conceived and does not take into account the realities of the payphone marketplace.

Section 276 of the 1996 Act requires that payphone providers receive “fair compensation” for all calls placed from their payphones. “Fair compensation” means fair to everyone – payphone providers, interexchange carriers, 800 subscribers and consumers. In light of the fact that the payphone market is not competitive, and that the market for coinless calls differs dramatically from the market for coin calls, it is clear that the Commission must abandon its attempt to treat the two markets similarly if it wants to withstand judicial scrutiny. Although the FCC may be eager to extract itself from its role as a regulator in the payphone market, for the present, the payphone market – at least the coinless market – requires the FCC’s continued regulation and guidance. Accordingly, the only fair approach to pricing coinless calls requires adopting an incremental cost-based rate, so that payphone providers receive a reasonable price for their services and 800 subscribers and other payphone users are not the only ones saddled with the cost.^{33/}

^{33/} If the Commission chooses to adopt a cost-based rate, it must be sure to base that rate on the costs of all payphone providers. Earlier in this proceeding, the Commission performed a cost-based analysis supposedly to confirm that its “market surrogate” for coinless calls was accurate. As has been pointed out numerous times by the Consumer-Business Coalition and others in this proceeding, however, the Commission’s cost-based analysis relied solely on data provided by independent payphone providers, who incur higher costs than the local exchange carriers that own the majority of the nation’s payphones. See, e.g., Consumer-Business Coalition

Finally, should the Commission amend its pricing methodology, and, as was explicitly contemplated by the D.C. Circuit, order payphone providers to pay refunds, it should specifically require IXCs to pass through the benefits of such refunds to 800 service subscribers.^{34/} The Commission currently permits IXCs to pass on the full cost of payphone compensation to 800 service subscribers and consumers, and it would manifestly unfair if IXCs were not required to provide these entities with any regulatory or court-ordered cost savings as well.

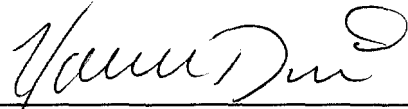
Comments at 5-6; AT&T Petition for Reconsideration, CC Docket No. 96-128 (filed Dec. 1, 1997) at 12-16. To arrive at a fair cost-based rate for pricing coinless calls, the Commission must take into account costs incurred by all payphone providers. Studies submitted by MCI and AT&T in this proceeding that take into account these costs suggest that an appropriate per-call compensation rate may be as low as \$0.06 per call. See First Report and Order at ¶ 42.

^{34/} The D.C. Circuit acknowledged that the FCC has the authority to require refunds. MCI Telecomm. Corp. at 7.

CONCLUSION

For the reasons described above, the Commission should pay attention to the D.C. Circuit's clear directive and abandon its effort to base the rate for 800 and access code payphone calls on the local coin rate. Instead, the Commission should adopt an incremental cost-based approach for pricing coinless calls that will withstand judicial scrutiny and be fair to payphone providers, carriers and users alike.

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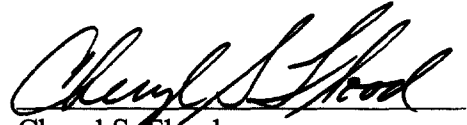
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Dated: July 13, 1998

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CERTIFICATE OF SERVICE

I, Cheryl S. Flood, hereby certify on this 13th day of July, 1998 that a copy of the foregoing "Comments of the Consumer-Business Coalition for Fair Payphone-800 Fees" was served on the following by hand:


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